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## Trade Regulation—Sherman Act—Rule of Reason Applied to Division of Territories.—United States v. Pan American World Airways

Carroll E. Dubuc

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year to which a liability is directly attributable to making services available. Thus, the new statute avoids one pitfall of section 452, that of cash basis taxpayers changing to an accrual basis and receiving a "double deduction" in the year of transition. To allay further the difficulty, a special transitional rule is provided by section 456. After an inclusion and deductions according to formula, the taxpayer is whole again at the end of five years.<sup>13</sup> Thus, for those taxpayers coming within the definition of "membership organization" in section 456, Congress has vindicated generally accepted commercial accounting practices for tax purposes where the courts have failed. However, it appears that there are businesses, not "membership organizations," which will continue to be bound by the decision in the present case. Thus, the U.S. Court of Appeals for the Eighth Circuit had held that an accrual-basis dance studio's receipts from instruction contracts could be spread over the tax years covered by the contract according to the number of lessons taught in each year where the student had executed a noncancelable contract and installment note. Also, the Seventh Circuit had held that an accrual-basis transit company could deduct each year its estimates of probable liability on unsettled, self-insured accident claims arising during the year. In light of its holding in the instant case, the Supreme Court by per curiam orders vacated and remanded in both cases.<sup>14</sup> Presumably neither these cases nor others of a similar nature are affected by section 456.

BRIAN E. CONCANNON

**Trade Regulation—Sherman Act—Rule of Reason Applied to Division of Territories.—*United States v. Pan American World Airways*.<sup>1</sup>—** Shortly after the first air mail contracts for South American service were

<sup>13</sup> "d) Transitional Rule.—

"(1) AMOUNT INCLUDIBLE IN GROSS INCOME FOR ELECTION YEARS.

—If a taxpayer makes an election under this section with respect to prepaid dues income, such taxpayer shall include in gross income, for each taxable year to which such election applies, not only that portion of prepaid dues income received in such year otherwise includible in gross income for such year an additional amount equal to the amount of prepaid dues income received in the 3 taxable years preceding the first taxable year to which such election applies which would have been included in gross income in the taxable year had the election been effective 3 years earlier.

"(2) DEDUCTIONS OF AMOUNTS INCLUDED IN INCOME MORE THAN ONCE.—A taxpayer who makes an election with respect to prepaid dues income, and who includes in gross income for any taxable year to which the election applies an additional amount computed under paragraph (1), shall be permitted to deduct, for such taxable year and for each of the 4 succeeding taxable years, an amount equal to one-fifth of such additional amount, but only to the extent that such additional amount was also included in the taxpayer's gross income during any of the 3 taxable years preceding the first taxable year to which election applies." *Supra* note 11.

<sup>14</sup> *Comr. v. Schlude*, 367 U.S. 911 (1961), reported below in 283 F.2d 234 (8th Cir. 1960); *Comr. v. Milwaukee & Suburban Transport Corp.*, 367 U.S. 906 (1961), reported below in 283 F.2d 279 (7th Cir. 1960).

<sup>1</sup> 193 F. Supp. 18 (S.D.N.Y. 1961).

granted by the Government in 1928,<sup>2</sup> W. R. Grace & Co., a steamship carrier with agencies on the west coast of South America, joined Pan American Airways in the organization of Pan American-Grace Airways, commonly known as Panagra. Each owned fifty per cent of this joint venture, and it was for expediency of operation that Pan American's "know-how" was combined with the economic advantage of Grace & Co.'s existing agencies. The U. S. Government approved Panagra's organization and granted it the air mail contract down the west coast of South America. At this time the government policy in promoting air mail carriage was to grant a single contract on each route. Subsequently, the two joint venturers agreed that the routes down the east and west coast of South America would remain divided and that Pan American would retain its exclusive service between the U. S. and the Canal Zone. Since the initial agreements, Grace & Co., through its stock representatives, and the U. S. Government, through the Civil Aeronautics Board,<sup>3</sup> have deemed it desirable to allow Panagra to petition for an extension of its west coast routes to include a U. S. terminal, but Pan American has opposed such application by exercising the pocket veto of its negative stock control. This suit was brought by the Government Anti-Trust Division upon the request of the CAB against Pan American Airways, W. R. Grace & Co., and Pan American-Grace Airways, jointly and severally, for violations of sections 1, 2, and 3 of the Sherman Antitrust Act<sup>4</sup> after

<sup>2</sup> In 1929 substantially all transportation between the U.S. and Latin America was by steamship, and air carriers of that era were faced with a difficult task in attempting air service competition because no operational facilities existed in Latin America. Without U.S. Government mail contracts to subsidize expansion and revenue, no airline could economically survive in the pioneer Latin American venture, although the U.S. Government was desirous of establishing American Flag carriers on South American routes. As a result of this policy, and because economic subsidization was necessary, the U.S. Government granted Pan American World Airways several contracts for mail carriage from the U.S. to the Canal Zone and through to the east coast of South America. At this time no air service was available to the west coast of South America.

<sup>3</sup> Under the Civil Aeronautics Act of 1938, 52 Stat. 977 (1938), as amended, 49 U.S.C. § 401 et seq. (1958), the Civil Aeronautics Board was organized and given primary jurisdiction over matters of air commerce relating to route approval and franchising, between carriers affecting commerce, and acquisitions by carriers. Thus, primary jurisdiction was raised by Pan American in its post-trial brief, but only that portion relating to route evaluation and extension was deferred to the CAB by the court. *U.S. v. Pan American World Airways*, supra note 1, at 28. Under the Sherman Act a district court retains primary jurisdiction when monopolization is part of the charge since much of the subject matter is outside the scope of CAB authority and the remedy sought, divestiture of stock, is outside its power to order since the "grandfather-clause" of the Civil Aeronautics Act gives approval to corporate structures existing prior to 1938 and makes them immune from divestment orders of the Board.

<sup>4</sup> The Sherman Act, 26 Stat. 299 (1890), as amended, 15 U.S.C. §§ 1-3 (1958).

§ 1. Every contract, combination in the form of trust or otherwise, or conspiracy in restraint of trade or commerce among the several states, or with foreign nations is hereby declared to be illegal. . . .

§ 2. Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several states, or with foreign nations shall be deemed guilty of a misdemeanor. . . .

several CAB hearings failed to result in a solution.<sup>5</sup> HELD: The joinder of Grace & Co. and Pan American and the incident division of territories agreement was not a conspiracy to restrain competition under section 3,<sup>6</sup> nor an unlawful, per se, restraint of trade under section 1,<sup>7</sup> but the suppression by the parent airline, Pan American, through its failure to approve its subsidiary's efforts to extend its South American service to the U. S., constituted a monopolization of commerce in contravention of section 2 of the Sherman Act.<sup>8</sup> The court dismissed the complaint against W. R. Grace & Co. and Panagra Airways Inc., and granted a decree enjoining Pan American from interfering with Panagra's application for a U. S. terminal, and ordering it to show cause why such final decree should not contain a provision directing it to divest itself of its Panagra stock.<sup>9</sup>

The court was faced with one of the dilemmas in the twilight zone of antitrust law, i.e., how to enforce the intent of Congress expressed in the Sherman Act and still give at least token effect to the present American State Department policy<sup>10</sup> of inducing investment of private capital in international ventures in underdeveloped areas by giving some judicial guarantee to the investor that he will not eventually be divested of his

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§ 3. Every contract, combination in form of trust or otherwise, or conspiracy, in restraint of trade or commerce in any Territory of the United States or of the District of Columbia, or in restraint of trade or commerce between such territory and another, or between any such territory or territories and any state or states or the District of Columbia, or with foreign nations, or between the District of Columbia and any state or states or foreign nations is hereby declared illegal.

<sup>5</sup> Panagra Terminal Investigation, 4 CAB 670 (1942), rev'd in *W. R. Grace & Co. v. C.A.B.*, 154 F.2d 271 (2d Cir. 1946), cert. granted, *Pan American Airways Corp. v. W. R. Grace & Co.*, 328 U.S. 832 (1946), dismissed as moot, 332 U.S. 827 (1947); *Latin American Air Service Case*, 6 CAB 857 (1944). Cf. *Local Feeder and Pick-up Air Service Case*, 6 CAB 1 (1946), and *New York Balboa Through Service Reopened*, 18 CAB 501 (1958). Subsequent to the Through Flight Agreement approved by CAB in 1946, 8 CAB 50 (1946), between Pan American and Grace which allowed Panagra crews to fly Pan American planes through to New York and Miami, Grace filed an application on behalf of Panagra for a terminal franchise in Miami, New York and the west coast of the United States. The action on this petition has been suspended pending the outcome of this case brought by the United States, and therefore Judge Murphy has left the determination of various facets of the application to the CAB when the case is heard, *United States v. Pan American World Airways, Inc.*, supra note 1, at 23, 45.

<sup>6</sup> *United States v. Pan American World Airways, Inc.*, supra note 1, at 32.

<sup>7</sup> *Id.* at 33.

<sup>8</sup> *Id.* at 35, 39.

<sup>9</sup> It was also held that Grace & Co.'s stock ownership in Panagra does not per se violate the Sherman Act. The court, relying on *United States v. Inter Island Steam Navigation Co.*, 87 F. Supp. 1010 (D. Haw. 1950), a factually similar case except that no domestic United States monopolistic restraint was alleged. The government has appealed the dismissal against W. R. Grace & Co. and Panagra directly to the U.S. Supreme Court, and Pan American has filed a cross appeal to the judgment to show cause. 30 U.S.L. Week 3041 (Aug. 1, 1961).

<sup>10</sup> Report of the Attorney General's National Committee to Study the Antitrust Laws, 90 et seq. (1955).

holdings.<sup>11</sup> The U. S. is playing an increasingly important role in the economic growth of less developed countries—mainly by encouraging private investment of capital.<sup>12</sup> Its competitors, such as the Soviet Union, on the other hand, have made foreign commercial operations by the government an integral part of their foreign policy. Many of our close allies have not only approved such foreign operations, but have specifically exempted foreign commerce from the effect of the Fair Trade Practice Laws.<sup>13</sup>

The present state of the law with regard to violations of the Sherman Act does not condemn joint venture operating agreements by American corporations in underdeveloped countries<sup>14</sup> unless they involve specific restrictive features, such as elimination of competition by merger with existing competitors to suppress possible competition,<sup>15</sup> price fixing,<sup>16</sup> or division of territories.<sup>17</sup> The per se condemnation of these restraints is the traditional interpretation of section 1 of the Sherman Act.<sup>18</sup> Should this interpretation remain the judicial standard, the problems of inducing foreign investment and joint operation would become acute. Many writers have commented to this effect with various solutions having been offered, including recommendations for Congressional legislative exemption or executive exemption by treaty.<sup>19</sup> However, since the Sherman Act has historically and tra-

<sup>11</sup> Friedmann, *Antitrust Law and Joint International Business Ventures in Economically Underdeveloped Countries*, 60 *Colum. L. Rev.* 780 (1960).

<sup>12</sup> The World Bank, International Finance Corporation, Inter American Development Bank, United States Import-Export Bank, Development Loan Fund, and the International Cooperation Administration all show government activity in this field, yet the actual investments and operations abroad are all carried on by private capital in the form of joint ventures.

<sup>13</sup> United Kingdom; Restriction Trade Practices Act of 1956, 4 & 5 *Eliz. 2*, ch. 68. West Germany; Act of July 27, 1957, *Bundesgesetzblatt* pt. 1 at 1181 (Ger.).

<sup>14</sup> *United States v. E. I. DuPont de Nemours & Co.*, 118 F. Supp. 41, 220 (D. Del. 1955); *Foundry Services, Inc. v. Beneflex Corp.*, 110 F. Supp. 857 (S.D.N.Y. 1952), rev'd on other grounds, 206 F.2d 214 (2d Cir. 1953); *United States v. Imperial Chem-Industries, Ltd.*, 100 F. Supp. 504 (S.D.N.Y. 1951); *United States v. Inter Island Steam Navigation Co.*, supra note 9.

<sup>15</sup> *United States v. Minnesota Mining & Mfg. Co.*, 92 F. Supp. 947 (D. Mass. 1950).

<sup>16</sup> *Timken Roller Bearing Co. v. United States*, 83 F. Supp. 284 (N.D. Ohio 1949), aff'd, 341 U.S. 593 (1951).

<sup>17</sup> *Timken Roller Bearing Co. v. United States*, supra note 16; *United States v. National Lead Co.*, 63 F. Supp. 513 (S.D.N.Y. 1945), aff'd, 332 U.S. 319 (1947).

<sup>18</sup> Judge Taft adopted this approach in *United States v. Addyston Pipe & Steel Co.*, 85 Fed. 271 (6th Cir. 1898), aff'd, 175 U.S. 211 (1899). His view was that if there were direct restraints of trade such as price-fixing agreements, suppression of competition by merger of competitors, or division of territories, then a court could not consider the economic rationale behind such agreements nor their practical necessity, but must instead condemn them as per se violations of the Sherman Act which prohibits "every" restraint of trade. However, if the restraints were ancillary to the commercial purpose, then he felt that the court might consider practical and economic justifications. See note 3 supra. *Southern Pacific Co. v. United States*, 259 U.S. 214 (1921); *United States v. Chicago Board of Trade*, 246 U.S. 231 (1918); *United States v. Union Pacific R.R. Co.*, 226 U.S. 61 (1912); cf. *Northern Securities v. United States*, 193 U.S. 197 (1903).

<sup>19</sup> Note, *Jointly Owned Companies Operating Abroad; A Problem in Antitrust Policy*, 47 *Geo. L.J.* 125 (1956), Brewster, *Antitrust and American Business Abroad*

ditionally been the subject of much "judicial legislation," due to the factually unique nature of each antitrust suit, it would seem that the better solution lies in an application of a "rule of reason" doctrine, rather than further limitation by statute<sup>20</sup> in a field of constantly fluctuating circumstances. Several cases have suggested such an approach in lucid dicta.<sup>21</sup> The most potent language to this effect is found in Mr. Justice Jackson's vigorous dissent in *Timken Roller Bearing Co. v. United States*,<sup>22</sup> where he criticizes the failure of the majority to consider the economic necessity for the division of territories in a highly competitive and unstable foreign venture:

It is one thing for competitors . . . to divide the United States Market which is an economic legal unit; it is another for one industry to recognize that foreign markets consist of many legal and economic units and go after each through separate means. I think this decision will restrain more trade than it sets free.<sup>23</sup>

The approach taken by Judge Murphy in *Pan American* would seem to parallel this view. He has considered the nature of air carrier operations, the conditions existing at the time the restrictive agreements were made, the economic purpose of the restraints, the position of the companies, the effect on domestic markets, and the competitive relationship between the ventures, Pan American and Grace Co. in 1929, and the fact that this venture was the proximate result of government-promoted activity. All of these factors were relevant to determination of the effect of the restraints on the public interest. This exhaustive examination of the facts resulted in an equitable though noticeably unsubstantiated decision. The judge has tacitly applied a rule of reason to division of territories activity, and, in so doing, removed such restraint on competition from the per se condemnation of the past in deference to the foreign economic promotion policy of the State Department. The decision is not startlingly unique, but it purports,

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(1958); Antitrust Law and Joint International Business Ventures in Economically Underdeveloped Countries, *supra* note 10; Report of Attorney General's National Committee to Study the Antitrust Laws, *supra* note 10, at 77 et seq.; Hearings Before the Antitrust Subcommittee on the Judiciary, 84th Cong., 1st Sess. § 3.1, pp. 263-64 (1955).

<sup>20</sup> One of the statutory exemptions to the Sherman Act, § 1 of the Webb-Pomerene Act, 40 Stat. 516 (1918), as amended, 15 U.S.C. § 61 (1958), allows price stabilization agreements in the export trade so long as such agreements do not injure nonparticipating competition or trade in the domestic markets.

<sup>21</sup> See, e.g., Mr. Justice Brandeis' opinion in *United States v. Chicago Board of Trade*, *supra* note 18, at 238: "The true test of legality is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition or whether it is such as may suppress or even destroy competition. To determine that question the court must ordinarily consider the facts peculiar to the business to which the restraint is applied; . . . the nature of the restraint, and its effect, actual or probable." In *United States v. Aluminum Co. of America*, 148 F.2d 416, 443 (2d Cir. 1945), in treating the jurisdiction problem, Judge Hand hinted that, although the Sherman Act did reach foreign agreements and cartels, it was the intent of Congress to treat such "outside" conduct differently so long as it was not intended to effect domestic commerce.

<sup>22</sup> *Supra* note 16.

<sup>23</sup> *Id.* at 608. See also Mr. Justice Frankfurter's dissent, *id.* at 605.

without so stating, to suggest a judicial answer to "the foreign joint venture without antitrust risk" dilemma. This treatment is a throwback to the "undue restraint" test applied to alleged violations of section 2 of the Sherman Act in *Standard Oil Co. of N. J. v. United States*.<sup>24</sup> The substantive effect of this decision is the doctrine that so long as the facts indicate that the original foreign venture was lawful and not in restraint of trade, and so long as its ultimate effects are in accordance with a government policy to promote economic development abroad, the Sherman Act interpretation of section 1 condemning "every" direct restraint as per se illegal will not be applied.

The court did find, however, that Pan American's suppression of Panagra's extension to the U. S. violated section 2 of the Sherman Act. This finding appears warranted, but the possible remedy of divestiture is unusual.<sup>25</sup> In most of the cases in which divestiture or dissolution has been ordered, there has initially been a wrongful or illegal acquisition of the subject of the divestiture.<sup>26</sup> Ordinarily, the courts, having found the monopoly power and intent to control, have had a tendency to avoid ordering a structural change.<sup>27</sup> Thus, a rule of reason principle is also applied in section

<sup>24</sup> 221 U.S. 1 (1911), reiterated and clarified in *American Tobacco Co. v. United States*, 221 U.S. 196 (1911). There the court felt that the Sherman Act was a codification of the common law, well known to the almost unanimous attorney representation in Congress in 1890, in that the common law condemned only "undue" restraints of trade or those restraints which caused substantial damage to competitors. Cf. Litwin, Congress and the Sherman Antitrust Law 1887-1890, 23 U. Chi. L. Rev. 221 (1956). It therefore applied a rule of reason by interpreting economic factors, size and amount of competition, and volume of business in determining whether there was an "undue" restraint. Cf. *United States v. United Shoe Machinery Corp.*, 110 F. Supp. 295, 341 et seq. (D. Mass. 1953).

<sup>25</sup> The finding of monopoly powers and the intent to monopolize may be inferred from the pattern of a corporation action. If there is no monopoly power, *United States v. E. I. DuPont de Nemours & Co.*, 118 F. Supp. 41 (D. Del. 1953), aff'd, 351 U.S. 377 (1956), nor intent to monopolize, *United States v. Aluminum Co. of America*, supra note 21, then the charge under § 2 of the Sherman Act is not substantiated. Cf. *United States v. American Tobacco Co.*, supra note 18; *United States v. United Shoe Machinery Corp.*, supra note 24. Even when both of these elements are present, however, the remedy must be made to fit the wrong. In monopoly situations, since the wrong has already been accomplished, and size and control cannot practically be enjoined, divestiture is the only effective remedy. See *United States v. Aluminum Co. of America*, supra note 21.

<sup>26</sup> *United States v. Paramount Pictures Inc.*, 334 U.S. 131 (1948); *United States v. Yellow Cab Co.*, 332 U.S. 218 (1946); *United States v. Union Pacific R.R. Co.*, supra note 18; *United States v. Reading Co.*, 226 U.S. 324 (1912); *American Tobacco Co. v. United States*, supra note 24; *Standard Oil of New Jersey v. United States*, supra note 24; *Northern Securities v. United States*, supra note 18.

<sup>27</sup> Perhaps this is the result of unconsciously heeding Judge Wyzanski's caveat in *United States v. United Shoe Machinery Corp.*, supra note 24, at 347, 348:

Judicial decrees must be fitted into the framework of what a busy, and none too expert, court can supervise. Above all, no matter with what authority he is invested, with what facts and opinion he is supplied, a trial judge is only one man, and should move with caution and humility.

That considerations of this type have always affected anti-trust courts is plain from the history of the *Standard Oil*, *American Tobacco*, and *Alcoa* cases.

## CASE NOTES

2 cases in the framing of the remedy. Although divestiture was not actually ordered by Judge Murphy, it is felt that if this is the ultimate intent of the decision, such a sweeping decree should not be ordered without a closer scrutiny of precedent and the economic effects which might result. If the only Sherman Act violation was suppression of Panagra's application, it would appear that a mandatory injunction for allowance of such application, supervised not only by the courts, but by the interested joint venturer, Grace & Co., would solve the problem without the necessity of a speculative divestment.

CARROLL E. DUBUC

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To many champions of the anti-trust laws these cases indicate judicial timidity, economic innocence, lack of conviction, or paralysis of resolution. Yet there is another way of interpreting this judicial history. In the anti-trust field the courts have been accorded, by common consent, an authority they have in no other branch of enacted law. . . . They would not have been given, or allowed to keep, such authority in the anti-trust field, and they would not so freely have altered from time to time the interpretation of its substantive provisions, if courts were in the habit of proceeding with the surgical ruthlessness that might commend itself to those seeking absolute assurance that there will be workable competition, and to those aiming at immediate realization of the social, political, and economic advantages of disposal of power.

Cf. *United States v. National Lead Co.*, 332 U.S. 319, at 353:

It is not for the courts to realign and redirect effective and lawful competition where it already exists and needs only to be released from restraints that violate the antitrust laws. To separate the operating units of going concerns without more supporting evidence than has been presented here to establish either the need for, or the feasibility of, such separation would amount to an abuse of discretion.

A court may accept the injunction remedy because it is able to predict its effect towards improving competition, while it rejects the divestiture remedy because it feels that its limited economic background makes an order of structural change a very speculative decree in that its ultimate effect on competition cannot be predicted.